TC02105

Appeal number: TC/2010/8417

VAT – disallowance of input tax claim – question of fact whether expenditure used or to be used for purpose of business – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

DARRAGH HOUSE LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE BARBARA MOSEDALE

Sitting in public at Bedford Square London on 17 May 2012

Mr S Reeves, director, for the Appellant

Miss L Ratnett, HMRC officer, for the Respondents

DECISION

1. Darragh House appealed against assessments dated 12 January 2010 for repayment of input tax which HMRC considered was incorrectly reclaimed by the Company in its VAT returns for the periods 07/06 to 10/09. The review decision dated 14 July 2010 resulted in a reduced assessment.

2. The original assessments were for £8981.00 and £1371.00 (total £10,352). The review decision 14 July 2010 modified the assessments to a total of £9823. After the appeal was lodged the amounts HMRC considered due for 04/07 to 10/09 were further reduced on the basis of information provided by the appellant although this was never formalised in reduced assessments. By the time of the hearing HMRC considered that that what was in issue was some £3,076 for 04/07 to 10/09 (and an appropriate percentage of the input tax reclaimed in 07/06 to 01/07).

3. The appeal was lodged out of time but HMRC raised no objection to this and I admitted the appeal as it had been clear to HMRC that the appellant was disputing the assessments.

The facts

4. Evidence was given by Mr S Reeves, the director and shareholder of the appellant. Evidence on behalf of HMRC was given by Ms Joanne Shuttleworth who was the VAT officer who carried out the inspection and Ms Sarah Bates, who carried out the review.

5. From this evidence I find the following facts:

6. Mr Reeves is a surveyor. He chooses to operate his business via limited companies. Each "project", being the development of land, is owned by a different company. In jargon, it is referred to as a special purpose vehicle or SPV.

7. One company which was a constant was Darragh House Limited. All the work is done by this company and re-charged to the relevant SPV by way of management charges.

8. Mr Reeves evidence, which I accept and which was not challenged by HMRC, is that business is cyclical and sometimes very profitable with a lucrative project running. At other times, like now, there are no lucrative projects and the business is surviving on the profits made in earlier periods.

9. As a result of this cyclical nature, for some time the company submitted VAT input tax claims while declaring virtually no output tax. A visit by HMRC officer Joanne Shuttleworth took place in November 2009. At that point the business had been showing virtually nil output tax for 4 years. The situation had not changed at the date of the hearing.

10. At the visit Mr Reeves produced the original receipts for the input tax claims for periods 07/08, 10/08, 1/09, 4/09, 7/09 and 10/09. Later he produced them for earlier periods. He was unable to produce and has never produced the receipts for 01/07, 10/06 and 07/06 as these were in store.

11. And the assessments the subject of this appeal were the result of that visit.

12. In the event, explanations provided by Mr Reeves has led HMRC to revise the assessments as mentioned above. In particular, HMRC accepted that Darragh House was genuinely incurring input tax on supplies to be made to an SPV which under the contract with the SPV were not to be charged to the SPV until the property owned by the SPV was sold. The property currently is let. HMRC have allowed the Company to recover the input tax attributable to the services supplied to this SPV which are yet to be charged to them

13. After the information provided by Mr Reeves the assessments were reduced as noted above. As at the date of the appeal the remaining input tax in dispute was of 6 main types, as follows:

- Invoices not addressed to Darragh House
- Maintenance of "Redcar" telephone associated with alarm system;
- Car park charges
- Subsistence expenses;
- Business entertainment;
- Miscellaneous.

Invoices not addressed to Darragh House Limited

14. It was not in dispute that the appellant had reclaimed VAT on invoices which were addressed to other companies, principally Saga Property Services Ltd. The amount in dispute was some £2,367.14 so this was by far the largest element remaining in dispute.

15. As a matter of law, s 24(1) Value Added Tax Act 1994 provides:

> "… 'input tax', in relation to a taxable person, means the following tax, that is to say –
>
> (a) VAT on the supply to him of any goods or services….
>
> being …goods or services used or to be used for the purpose of any business carried on or to be carried on by him."

16. Mr Reeves was aggrieved because the invoices were addressed to one of his SPVs, in this case Saga Property Services Ltd, and Saga was VAT registered. We accept his evidence that it was a mistake that Darragh House had reclaimed the VAT:

Saga should have done but had not. As far as Mr Reeves was concerned it was merely a book entry error and HMRC had lost nothing as Saga (he said) was fully taxable and entitled to reclaim its input tax. At the outset, he said, he had asked for HMRC's advice on how to put the matter right but had not receive any help in putting matters right.

17. But that does not affect the position with regards Darragh House: the input tax was Saga's and therefore Darragh House should not have reclaimed it. It was not input tax used by the appellant for the purpose of any business carried on by it; nor did it hold the correct documentary evidence (an invoice addressed to Darragh House) in order to be able to reclaim it.

18. I dismiss the appeal on this point.

19. I sympathise with Mr Reeves' position: the appellant must repay the tax Saga may now be out of time to lodge its reclaim. Saga is not the appellant here and I can make no ruling on this nor were any arguments addressed to me on it. I merely draw to the attention of both parties that the provisions of Regulation 29 VAT Regulations 1995/2518 are that the time limits start to run from when the taxpayer "holds" the invoice. There may be a question here whether Saga could be said to "hold" the VAT invoices in question at a time when the appellant had included them in its records for the purpose of its own VAT reclaim.

20. But whatever is the answer to this question, so far as the appellant is concerned its appeal in respect of VAT on invoices addressed to other persons is dismissed.

Redcar alarm system

21. It was Mr Reeves' evidence which I accept that because his contents insurance at Darragh House had to include business cover for the office, it was a requirement of his insurers that he install and maintain a "Redcar" system. I was informed that this system involved a telephone call being made automatically if the burglar alarm at the house was tripped. The call was to a manned centre, whose response to the automatic phone call would be to ring the nominated key holder on the policy. The key holder (Mr Reeves' neighbour) would be asked if there were visible signs of entry: if there were the manned centre would place an emergency call to the police. The Redcar was expensive as not only did the phone have to be installed but there was an annual maintenance charge. It was the VAT on this annual maintainance charge that the appellant sought to reclaim and HMRC disallowed.

22. It was not clear to me or to Mr Reeves why this gave him better protection than simply having an ordinary burglar alarm: it was his evidence, which was not challenged by HMRC and which I accept, that he only installed it because it was a condition of the insurance policy and that that condition was only imposed because Mr Reeves' home was also the company's business premises. It was therefore his case that the costs of maintaining the Redcar phone line was exclusively a business expense and should be allowed in full.

23. HMRC, on the other hand, said they were prepared to allow him 50% on the basis of mixed business and private use under s24(5) VATA. They pointed out that Mr Reeves had not produced any documentary evidence that the Redcar system was fitted as a requirement of having business premises insurance.

24. Mr Reeves accepted, and I find, that if the burglar alarm was tripped in the domestic part of the house, it would benefit from the Redcar system as the automatic phone call to Redcar would be made whether the alarm was tripped in the domestic or business part of the property.

The law

25. Section 24(5) VATA provides:

> "Where goods or services supplied to a taxable person … are used or to be used partly for the purposes of a business carried on or to be carried on by him and partly for other purposes, VAT on supplies… shall be apportioned so that only so much as is referable to his business purposes is counted as his input tax."

Conclusion

26. I accept the oral evidence of the appellant. The input tax incurred by the appellant in respect of the Redcar system, was I find, incurred because otherwise the appellant could not insure its business premises. I am satisfied that Mr Reeves would not have installed the Redcar system were it not a condition of the appellant's insurance policy.

27. Therefore, the installation of the Redcar system was used for the purpose of the appellant's business and not used for any other purpose and in particular not for a private purpose of Mr Reeve's. While there was incidental benefit to Mr Reeves, in that his domestic accommodation as well as the appellant's business premises, had the benefit of the Redcar system, this was not the purpose for which it was used. Its purpose was to obtain insurance for the business premises.

28. I agree with and follow the decision of the VAT & Duties Tribunal where a similar issue arose (on very different facts) in the case of *Thorpe Architecture Ltd* (1992) VTD 6955. I agree with the statement of the chairman:

> "Expenditure incurred wholly for business purposes may produce an incidental benefit of a personal or non-business kind but it does not thereby lose the character of business expenditure…"

29. I allow the appeal in relation to the expenditure on the maintenance of the Redcar system.

Car park charges at airports

30. Mr Reeves' evidence was that these charges were incurred when he parked at the airport car park to use the mainline railway line to travel into London for business

meetings, or when he picked someone up for a business meeting from the airport or airport station. He pointed out that all charges were short-stay incurred Monday-Friday in the day time and it was not a case of him parking his car while he was on holiday for two weeks.

31. It was his evidence that he frequently travelled to London on business and would not have travelled to London Monday-Friday other than for business. He said he attended meetings connected with existing or potential future projects. This evidence was not challenged and I accept it.

32. I was not shown the actual receipts.

33. He complained that HMRC were inconsistent in that they had allowed the Company's other parking expenses but just disallowed it where the car park used was at an airport, even though both airports used were also mainline stations.

34. HMRC did not challenge Mr Reeves' evidence on this but maintained that the VAT should be disallowed on the basis Mr Reeves had not shown sufficient detail for them to be satisfied that it was money spent exclusively on business purposes.

35. I accept the appellant's evidence that the car parking expenses were incurred for business purposes (business meetings) and therefore the appeal is allowed in relation to the VAT on the car parking charges.

Subsistence

36. Mr Reeves' case was that these receipts fell into two categories. Sandwiches at motorway service stations and meals at Little Chefs when he was travelling on business and meals on a Friday night in a local restaurant when Mr Reeves and his company secretary (his wife) ate out and, he said, discussed the business.

37. Mr Reeves accepted that the latter receipts were not business expenses but says at the time, and before Ms Shuttleworth explained it to him, he had not understood this. He accepted that it was right that the input tax on the local subsistence should be disallowed but considered he was still entitled to reclaim the VAT in so far as he was buying sandwiches while travelling on business.

38. Taxpayers can only recover expenses "used or to be used for the purpose of any business" (S 24 VATA 94 as cited above). Lunch expenses for employees and directors of a taxpayer are ordinarily not for the purpose of the business as it is simply necessary for people to eat.

39. As accepted by all parties, the Company is not allowed local subsistence costs, even if business was discussed: a business meeting could have easily been held at the office and the fact it was not means that the purpose of the meal out was more than to discuss the business.

40. It is only where an employee or director is forced by the needs of business to purchase food it would not otherwise have done, such as when travelling for business, that the expense may be said to be for the purpose of the business.

41. Mr Reeves did not bring the receipts with him. From HMRC's schedule I can see that some of these expenses are labelled "local subsistence" and some "subsistence". the appellant agrees it is not entitled to the VAT labelled "local subsistence". On those labelled "subsistence", the VAT involved is small sums (between £0.58 and up to £18). Mr Reeves suggests they were largely receipts from motorway service stations: Ms Shuttleworth's recollection is that the receipts were largely from restaurants and pubs.

42. Bearing in mind the diversity in the sums involved I can discern that they cannot largely be just sandwiches from motorway service stations and therefore on this I find Mr Reeves' recollection is faulty. Therefore, I conclude that the appellant has not made out its case that these expenses were business expenses rather than Mr Reeves just choosing to have a meal out.

43. I dismiss the appeal on this point.

Business entertainment

44. The appellant recovered 35% of the VAT on invoices which related to business entertainment. He said he recovered 35% because he had been advised this was the right thing to do by HMRC as he was entitled to recover the subsistence element of entertainment.

45. I am not concerned (having no judicial review powers) with what HMRC said to Mr Reeves. It is certainly not the law that a taxpayer is entitled to recover VAT on all subsistence expenses for its employees. Outside the context of business entertainment, it can recover VAT incurred on feeding its employees only where the expenditure was incurred for a business purpose. Within the context of business entertainment the input tax is blocked, unless it is staff rather than business entertainment (*Ernst & Young* VTD 15100) as the Value Added Tax (Input Tax) Order 1992 provides:

> "5(1) Tax charged on any goods or services supplied to a taxable person, …is to be excluded from any credit under section 25 of the Act, where the goods or service in question are used or to be used by the taxable person for the purposes of business entertainment."

46. I was given no evidence on the nature of these supplies other than the appellant accepted that they were for business entertainment. The VAT incurred in respect of them is therefore blocked from recovery and the appeal dismissed in so far as it relates to business entertainment.

Miscellaneous

47. HMRC's schedule showed that other sums of input tax had been disallowed. I note for instance that some £6.17 was disallowed on the basis it was Portugese VAT. If correct (and Mr Reeves did not suggest otherwise) this disallowance was plainly correct.

48. It was for the appellant to show me that HMRC was wrong to disallow this input tax. I accept his evidence that the expenses in relation to the fridge, torch, engineer and lazer level were for the purpose of the appellant's business as provider of management services. From what little information I was given, I was not satisfied that the other expenses were business expenses.

49. In respect of the various miscellaneous items I allow the appeal to the extent stated above. but not otherwise.

Quantum

50. As Mr Reeves produced no records for the earliest three quarters, the assessments for the periods 07/06 to 01/07 were estimates based on the percentage of overclaimed input tax in the other periods of the assessment. As HMRC accepted at the hearing, the percentage used to calculate these assessments must be revised to take account of the reductions in the assessments for the later periods where records are available: the percentage must be reduced to reflect the reductions allowed by HMRC before the commencement of the hearing and the reductions allowed by me in this decision notice.

51. This decision is therefore, in respect of periods 07/06 to 01/07 one of principle only. If the parties are unable to agree the quantum of the assessment for these three quarters, either is at liberty to revert to the Tribunal for a ruling.

52. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

BARBARA MOSEDALE
TRIBUNAL JUDGE

RELEASE DATE: 27 June 2012